

Cite as Det. No. 05-0377R, 27 WTD 61 (2008)

BEFORE THE APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

In the Matter of the Petition For Correction of )	<u>D E T E R M I N A T I O N</u>
Assessment and Refund of )	
)	No. 05-0377R
)	
)	Registration No. . . .
)	Doc. No. . . . /Audit No. . . .
)	Docket No. . . .

- [1] RULE 245; RCW 82.04.065: NETWORK TELEPHONE SERVICE – STATUTORY CONSTRUCTION – UNAMBIGUOUS STATUTE. RCW 82.04.065 is not an ambiguous tax imposing statute. It defines precisely the range of activity that falls within its purview -- the transmission of telephonic, video, data, or similar communication by telephone line or microwave.
- [2] RULE 155; RULE 245; RCW 82.04.065; ETA 544: RETAILING B&O TAX VS. SERVICE B&O TAX -- CLASSIFICATION OF INCOME – PRIMARY NATURE –TRANSMISSION OF DATA FOR HIRE VS. USE OF COMPUTER HARDWARE OR SOFTWARE TO FURNISH INFORMATION OR DATA. In determining the proper classification of a taxpayer’s income, we will consider the “primary nature” of the taxpayer’s activities. If the primary nature of the taxpayer’s activities was the transmission for hire of data via a telephone network or similar transmission system, including a satellite transmission system, the taxpayer’s income would be subject to retailing B&O tax, and the taxpayer would be required to collect retail sales tax from its customers. In contrast, if the primary nature of the taxpayer’s activities was the use of computer hardware or software to furnish information or data, the taxpayer’s income would be subject to service B&O tax. Although a taxpayer’s service may provide some information, this fact does not negate its classification as network telephone service.
- [3] RULE 155; RCW 82.04.297: INTERNET SERVICE – ACTIVITIES QUALIFYING AS. Because the primary nature of the taxpayer’s activity was network telephone service, its activity was not an “internet service.” Internet service includes only those persons who provide access to the internet. In this

case, the taxpayer did not provide access to the internet; its customers could simply use the internet to access the data the taxpayer transmitted.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

C. Pree, A.L.J -- A taxpayer engaged in the business of selling a satellite-based tracking and communications system that includes instant messaging and position reporting between vehicles in transit and their dispatch centers petitions for reconsideration of Det. No. 05-0377. In that determination, we concluded that the taxpayer's income derived from network telephone service and, accordingly, was subject to retail sales tax and retailing B&O tax. On reconsideration, the taxpayer again contends its income should be taxed under the service classification as either information or internet service. We conclude that Det. No. 05-0377 correctly determined that the taxpayer's income is properly taxed under the retailing classification as network telephone service. Accordingly, we deny the taxpayer's petition.<sup>1</sup>

#### ISSUES:

1. Whether Det. No. 05-0377 erred in failing to conclude that RCW 82.04.065 is an ambiguous tax-imposing statute that should be construed in favor of the taxpayer.
2. Whether Det. No. 05-0377 erred in failing to conclude that the primary nature of the taxpayer's service was "information service."
3. Whether Det. No. 05-0377 erred in failing to consider whether the primary nature of the taxpayer's service was "internet service."

#### FINDINGS OF FACT:

The facts were stated in detail in Det. No. 05-0377 and are summarized here, as clarified by the taxpayer in its reconsideration petition.

The taxpayer is engaged in the business of selling [a] service . . . . The service provides customers with a satellite-based tracking and communications system that includes instant messaging and position reporting between vehicles in transit and their dispatch centers. . . . The service relies upon data originating from the customers' trucks and dispatch centers, as well as information the taxpayer provides. The service allows transportation companies to maximize the use of their vehicles and drivers to haul loads more efficiently and safely.

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<sup>1</sup> Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

In addition to providing a vehicle positioning service, the service provides two-way messaging services, via telephone service and satellite, from the customer's vehicles' dispatch centers to the vehicles. The service allows drivers to type and read messages. On reconsideration, the taxpayer clarified that its service generates information that is passed from the trucks' terminals in the form of a data packet; it is not possible for the driver to send standard e-mails via the system. The taxpayer provides its customers with terminals for their trucks that contain terminal applications and modem software necessary for using the service. In addition, as a prerequisite for obtaining the service, the taxpayer's customers must purchase a software license, to be used at its dispatch center, from the taxpayer.

Messages are sent from the truck directly to a satellite. The satellite then sends the message to the [taxpayer's center] outside Washington. When the message is received at the [taxpayer's center] it is temporarily stored. The data is processed and reformatted into a customer-usable form at the [taxpayer's center] and additional information from the [taxpayer's center] is added. Such information includes the location of the vehicle and time and date stamps.

The taxpayer determines the location of the vehicle based on its proprietary technology; it is not based on information contained in data messages from the vehicle. A position is sent with every electronic message. If a message is not sent within . . . , an automated position report is sent by itself.

A communications link is required for the taxpayer's customers to access the data. Customers can arrange separately for their ability to access the [taxpayer's center] through their own Internet access or local dial-up service. Alternatively, customers can arrange to use the taxpayer's 800 line for a separate charge. In addition, the taxpayer arranged for third party communication links for some of its customers and separately billed them for these charges. The taxpayer's contract with its customers makes the customers responsible for the charges for the link between their dispatch centers and the [taxpayer's center]. If the customer chooses an internet link, the customer acknowledges that the taxpayer is not responsible for any break in service due to the customer's lack of internet access. If the customer chooses a dial-up or 800 service, the taxpayer [states that it has no warranty obligations with respect to the telephone ground link; however, it agreed to pass through to the customer any warranties provided by others.] On reconsideration, the taxpayer explained, "If the customer does not secure a third party to provide the communication network, then the [service] information service stops within [the taxpayer's] equipment."

Under the taxpayer's contract with its customers, customers may choose a base plan or enhanced plan. . . . Under either plan, customers may purchase additional messaging. . . . Position polls are provided with each additional message purchased. Customers may also purchase additional position polls (without messaging). The taxpayer also provides emergency, priority, and group messaging for additional charges. All of these charges are at issue.

The Audit Division of the Department of Revenue reviewed the taxpayer's records for the period of January 1, 1998, through September 30, 2001, and issued an assessment of \$ . . . , comprised of retail sales tax, retailing B&O tax, and interest. The taxpayer paid the assessment, plus additional interest and penalties, and requested a refund. Additionally, the taxpayer requested refund of additional amounts reported and paid under the retailing classification and retail sales tax on the taxpayer's excise tax returns through December 31, 2001.

On reconsideration, the taxpayer again argues that its services are properly classified as information or internet services, subject to service B&O tax, rather than retailing B&O tax and retail sales tax, as was included in the assessment.

#### ANALYSIS:

##### **1. Did Det. No. 05-0377 err in failing to conclude that RCW 82.04.065 is an ambiguous tax-imposing statute that should be construed in favor of the taxpayer?**

[1] In Det. No. 05-0377, we concluded that the taxpayer's service fit within the RCW 82.04.065 definition of "network telephone service" and, accordingly, its income from such service was subject to retail sales tax and retailing B&O tax. See RCW 82.04.050, .250; RCW 82.08.020. RCW 82.04.065 defines "network telephone service" in pertinent part, as follows:

"Network telephone service" means the providing by any person of access to a telephone network, . . . , or the providing of telephonic, . . . , data, or similar communication or transmission for hire, via a telephone network, toll line, . . . , or similar communication or transmission system. "Network telephone service" includes the provision of transmission to and from the site of an internet provider via a telephone network, toll line, . . . , or similar communication or transmission system.

The taxpayer argues that RCW 82.04.065 is an ambiguous tax imposing statute, which should be construed against the state and in favor of the taxpayer. Citing, e.g., *Simpson Inv. Co. v. Department of Rev.*, 141 Wn.2d 139, 149, 3 P.2d 741 (2000); *Ski Acres, Inc. v. Kititas County*, 118 Wn.2d 852, 857, 827 P.2d 1000 (1992).

In support of its argument that the statute is ambiguous, the taxpayer notes that the court in *Western Telepage Inc. v. City of Tacoma*, 140 Wn.2d 599, 988 P.2d 884 (2000), concluded that paging was properly included within the RCW 82.04.065 definition of "network telephone service," while the Department concluded it was not. Citing Tax Topics, June 1995. Although the taxpayer acknowledges that the Tax Topics article was retracted in a Special Notice dated April 2002, retroactive to July 1, 2000, the taxpayer nevertheless argues:

Regarding what activities fall within and without the statute, Western Telepage and the Department of Revenue have read the pertinent statute to exclude telepaging activity from

RCW 82.04.065. Tacoma and the courts have read the statute to include telepaging activity within RCW 82.04.065. Consequently, there is ambiguity in this statute and any construction of this statute should be construed in favor of the taxpayer.

However, the Washington Supreme Court in *Western Telepage* specifically addressed the issue of whether RCW 82.04.065 was ambiguous and concluded it was not. The court reasoned, “On its face, the statute is not ambiguous. It defines precisely the range of activity that falls within its purview -- the transmission of telephonic, video, data, or similar communication by telephone line or microwave.” 140 Wn. 2d at 608. In light of the Washington Supreme Court’s conclusion on this issue, we must similarly conclude that the statute is unambiguous and deny the taxpayer’s petition on this issue. *See also* Det. No. 02-0030E, 24 WTD 108 (2005).

**2. Whether Det. No. 05-0377 erred in failing to conclude that the primary nature of the taxpayer’s service was “information service.”**

[2] As we explained in Det. No. 05-0377, in determining the proper classification of the taxpayer’s income, we will consider the “primary nature” of the taxpayer’s activities. *See, e.g.*, ETA 544.04.08.245 (ETA 544); Det. No. 04-0023E, 23 WTD 206 (2004). On reconsideration, the taxpayer argues Det. No. 05-0377 erred in failing to conclude that the “primary nature” of its service is “information service,” taxable under the service classification. *See* RCW 82.04.290; WAC 458-20-155 (Rule 155). Under Rule 155 the term “information service” is defined as “every business activity, process, or function by which a person transfers, transmits, or conveys data, facts, knowledge, procedures, and the like to any user of such information through any tangible or intangible medium.”

Thus, if the primary nature of the taxpayer’s activities was the transmission for hire of data via a telephone network or similar transmission system, including a satellite transmission system,<sup>2</sup> the taxpayer’s income would be subject to retailing B&O tax, and the taxpayer would be required to collect retail sales tax from its customers. In contrast, if the primary nature of the taxpayer’s activities was the use of computer hardware or software to furnish information or data, the taxpayer’s income would be subject to service B&O tax. *See* Det. No. 90-128, 9 WTD 280-1 (1990).

On reconsideration, the taxpayer argues its service is properly classified as an information service because it allows customers to maximize their use of tractors and trailers to help prevent the hauling of empty trailers, thereby improving delivery times. Further, according to the taxpayer, the position location information is of “utmost importance” to the customers’ operations and the information the taxpayer’s service provides is the reason customers purchase the taxpayer’s services. Thus, contrary to the conclusion reached in Det. No. 05-0377, the taxpayer argues, “The

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<sup>2</sup> *See* Det. No. 88-193, 5 WTD 347 (1988); Det. No. 92-363, 12 WTD 519 (1992).

use of the satellite network is solely to complete the data link and is incidental to the true nature of the information services . . .”

However, we note that although the taxpayer’s service provides information, this fact does not negate its classification as network telephone service. Many network telephone services provide their customers with information the customers would not otherwise have. For example, the paging services at issue in *Western Telepage*, 140 Wn.2d 599, alerted customers that a person at a specific telephone number was trying to contact them, or provided a short text message. Despite the fact that the paging service provided customers with the information necessary to contact a specific person or provided a message the customer would not otherwise have, the court concluded that the paging service was network telephone service.

Further, the taxpayer argues, if its system “did not provide some greater value than the incidental telecommunications, then the customers would just use humans via cellular or land line telephones to communicate the information between the operating equipment and the terminal.” The “key element,” according to the taxpayer, is the information produced from the raw data generated by the trucks. The taxpayer reasons:

Without the hardware, software and proprietary technology to process, reformat and restructure the raw data, the transmission service is meaningless to customers. The . . . positioning report is the “information” and the real object of the service. Customers are paying for the vehicle position information that enables them to track the whereabouts and condition of their fleet at any time. If this was not critical to the customer, then they would use cell telephones or land line telephones to provide the information.

The fact that there is an alternative way to communicate does not negate the importance of the communication aspect of the taxpayer’s service. For example, in *Western Telepage*, the paging company’s customers could have purchased voice mail or used cell phones to enable their customers to contact them when they were not accessible by telephone. The fact that there were alternatives to paging did not compel the court to conclude that the taxpayer in *Western Telepage* was providing an information service, rather than a network telephone service.

In further support of its argument that its service is an information service, the taxpayer again cites Det. No. 98-202, 19 WTD 771 (2000). The taxpayer relied on this determination in its original petition, and we fully addressed its arguments in Det. No. 05-0377. However, in its reconsideration petition, the taxpayer further highlighted what it perceived to be four similarities between its facts and the facts in Det. No. 98-202:<sup>3</sup>

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<sup>3</sup> The taxpayer further argues that Det. No. 05-0377 erred in “implying” in its distinction of Det. No. 98-202 that Det. No. 98-202 involved one-way communication. We do not find such an implication in Det. No. 05-0377; however, we agree with the taxpayer that whether the communication is one-way or two-way is not dispositive. See *Western Telepage*, 140 Wn.2d at 610-11.

- Each requires telephone service to establish the connection in order to gain access to the information.
- Each provides information for customers to retrieve or access.
- The “true object” of each is information: Pricing and availability information in the case of the travel agency (Det. No. 98-202), and information regarding truck positioning and vehicle performance in the case of [the service offered by the taxpayer].
- Each stores information in the database for later retrieval.

We generally agree with the taxpayer’s first, second, and fourth points. However, we note that the importance of each of these elements in the two systems may vary widely. With respect to the third point, as we explained in Det. No. 05-0377 and further explain here, we disagree that the “true object” of the taxpayer’s service is the provision of information. This distinction is the key reason we reach a different result in this case than that reached in Det. No. 98-202. As we explained in our original determination, the reservation system in Det. No. 98-202 allowed access to a database of information from which to make reservations, while the taxpayer’s service primarily provides the medium for trucks and dispatch centers to communicate and send data.

The taxpayer next argues that Det. No. 05-0377 erred in concluding that the communications link is a part of its service. In our original determination, we concluded that the taxpayer was essentially engaged in a single activity—providing communication between customers’ trucks and their dispatch centers—that is not subject to bifurcation. On reconsideration, the taxpayer argues “The Determination turns the primary nature test upside down by using an incidental part of the . . . service to reclassify the primary activity of information services to network telephone business.” The taxpayer notes that because the communication link charges are clearly identified and billed, these charges should be separately classified as a distinct and separate transaction.

Contrary to the taxpayer’s assertion, Det. No. 05-0377 did not rest its conclusion regarding the proper classification of taxpayer’s service on the provision of the communications link. Instead, Det. No. 05-0377 reasoned that the furnishing of the satellite-based communication network is the “real object” of the transaction, and the positioning information is merely incidental to or part of the communication service being rendered. . . .

The taxpayer further argues the communications link is not necessary to receive its services. According to the taxpayer, other communication methods, such as fax, mail, phone calls, or e-mails can be used as an alternative to the communications link to deliver the information to customers. Thus, the taxpayer argues, the communications link is not a functionally integral part of the taxpayer’s service. We question the taxpayer’s assertion that these other communication methods are viable alternatives to the communications link, given the time-sensitivity of the data the taxpayer’s system transmits. Nonetheless, as we stated above, the fact that there may be alternative ways to communicate does not negate the importance of the communication aspect of the taxpayer’s service.

In our original determination, we found *Western Telepage*, 140 Wn.2d 599, persuasive. At issue in that case was whether the taxpayer's provision of paging services was subject to tax as network telephone service. The court concluded such services were properly classified as network telephone service because they transmitted data or similar communication by microwave. In other words, the taxpayer provided the medium over which the data was communicated. Similarly, we concluded, the taxpayer's services here primarily provide the medium for the transmission of messages.

On reconsideration, the taxpayer urges that *Western Telepage* is distinguishable because the taxpayer's service uses telecommunications as "the medium to transmit proprietary, . . . information to customers." Further, the taxpayer argues, it creates the information from raw data obtained from the customer's trucks, and:

It is this processed information that is valuable to the customer, not the raw data. For example, if the customer had the raw data, it would be impossible for the customer to know where its truck was located. The raw data means nothing to the customer. The . . . system is not merely a medium for communication; rather, it is a system used to acquire raw data which [taxpayer] uses to produce the information useful to customers. In contrast, *Western Telepage* provided the medium for customers to communicate.

Data conversion and protocol conversions occur in most, if not all, communication systems. These conversions, in and of themselves, do not mandate that the service be deemed an "information service." We applied this reasoning in Det. No. 00-159E, 20 WTD 372 (2001). In that determination, we concluded that where the taxpayer's network provided a computer data protocol conversion service in addition to transmitting data and information over its network to another computer, the true object of the service was the transmission of data and information and, accordingly, taxable as a network telephone service. We explained:

In this case, Taxpayer's protocol conversion services are additional services that allow the customer's transmitted data or information to interact with the receiving computer. It is functionally integrated with the transmission activities performed by Taxpayer's shared wide-area computer network. As such, it is an integral part of the transmission activity and cannot be bifurcated from what is essentially a single activity. This is true, even though the contract may or may not provide a basis for determining the value of the protocol conversion activity alone.

As we explained in detail in our original determination and in response to the taxpayer's arguments on remand, above, we conclude that the primary nature of the taxpayer's service is the furnishing of the medium over which the data is transmitted. The fact that the data must be converted to be useful does not change this result.



The taxpayer further takes issue with the following statement in our original determination: “Taxpayer clearly provided significant information services that enhanced the communications services. However, the taxpayer has failed to provide sufficient information from which we can conclude that the primary nature of its service is information services.” (Footnote omitted.) On reconsideration, the taxpayer states:

This is a puzzling assertion in that the primary nature is supported by [the service’s] billing statistics: [a relatively small percentage] of the charges were incremental messaging, the majority of which are macro messages which are restructured and reformatted and [the remainder] were position polls and other information. This ratio adequately supports the argument that the . . . service is primarily an information service.

This argument assumes that Det. No. 05-0377 concluded that the transmission of the position data did not constitute data transmission. Det. No. 05-0377 reached no such conclusion. To the contrary, the position data is an integral part of the data transmission activity that cannot be separated from what is essentially a single activity. *See* Det. No. 00-159E. This is true, even though the billing statements may or may not provide a basis for determining the value of position data alone. *See* Det. No. 00-159E. . . .

**3. Whether Det. No. 05-0377 erred in failing to consider whether the primary nature of the taxpayer’s service was “internet service.”**

[3] On reconsideration, the taxpayer argues Det. No. 05-0377 erred in failing to address why its service is not taxable as an internet service. Specifically, the taxpayer argues it provides internet service because the position information, date and time stamps, engine data, vehicle performance, trailer events, and driver performance reports are all processed and restructured information derived from raw data.

However, Det. No. 05-0377 did address this issue, albeit summarily. Specifically, in Det. No. 05-0377, we stated that because the primary nature of the taxpayer’s activity was network telephone service, its activity was not an “internet service.” We note that internet service, as defined in RCW 82.04.297, includes only those persons who provide access to the internet. Det. No. 01-036, 21 WTD 13 (2002). In this case, the taxpayer did not provide access to the internet; its customers could simply use the internet to access the data the taxpayer transmitted. Accordingly, we must deny the taxpayer’s petition on this issue.

**CONCLUSIONS OF LAW AND DISPOSITION:**

The taxpayer’s petition is denied.

Dated this 29<sup>th</sup> day of June, 2007.

